Fossil Group, Inc.
Q4 and Full Year 2024 Earnings Call Prepared Remarks
Wednesday, March 12, 2025

Christine Greany, Investor Relations:

Hello, everyone, and thank you for joining us. With me on the call today is Franco Fogliato, Chief Executive Officer and Andrew Skobe, Interim Chief Financial Officer.

Before we begin, I would like to remind you that information made available during this conference call contains forward-looking information and actual results could differ materially from those that will be discussed during this call. Fossil Group's policy on forward-looking statements and additional information concerning a number of factors that could cause actual results to differ materially from such statements is readily available in the Company's Form 8-K, 10-Q and 10-K reports filed with the SEC. In addition, Fossil assumes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise, except as required by law.

During today's call, we will refer to constant currency results, as well as certain non-GAAP financial measures. Please note that you can find a reconciliation of actual results to constant currency results and other information regarding non-GAAP financial measures discussed on this call in Fossil's earnings release, which was filed today on Form 8-K and is available in the Investors section on FossilGroup.com. There you will also find a supplemental presentation which outlines our Q4 results, turnaround plan and outlook.

With that, I'll now turn the call over to Franco.

Franco Fogliato, Chief Executive Officer:

We are pleased to have concluded the year with fourth-quarter results that exceeded our top and bottom-line guidance, as our early initiatives have already started to gain traction. Most notably, we expanded gross margins, reduced costs and delivered positive adjusted operating margins. I am incredibly grateful to our global teams for their hard work and dedication to Fossil Group.

During my first six months in the CEO role, we moved swiftly and took a number of pivotal actions to set up the business for long-term success while formulating a comprehensive turnaround plan. We are clear-eyed about the amount of work required to execute this turnaround and we are energized by the opportunity in front of us.

We have <u>tremendous</u> optimism and confidence in our ability to propel the business forward, fueled by our core foundational assets - iconic brands, innovative design, global reach, and talented teams. Fossil has a meaningful 40-year history of making watches accessible to consumers around the globe. We have unique design, manufacturing, and selling capabilities worldwide - in the Americas, Europe and Asia. Our strong brand equity is also reflected in our global industry rankings. Time Magazine ranked Fossil number #4 in 2024 in the global watch market and more recently, in late February, our Fossil Raquel Watch Ring was awarded Fashion Jewelry of the Year 2025 at the Inhorgenta Trade Show in Germany.

Our plans reflect the opportunity we see to unleash these assets and optimize them more effectively. We have moved quickly to implement change and create a path for the Company to return to profitable growth. We have introduced a turnaround plan centered on three primary pillars: Refocusing on our Core, Rightsizing our Cost Structure, and Strengthening our Balance Sheet.

Diving into our **first turnaround pillar** - **<u>refocusing on our core</u>**. This starts with building an operating model that is brand-led and consumer-focused. We are returning to our core with a renewed emphasis on traditional watches on our Fossil brand platform, as well as our go-to-market execution. We are well underway on four major initiatives:

- Launching a new Fossil brand platform
- Leveraging our core licensed brands, including Armani, Kors, and Diesel
- Optimizing our global wholesale footprint, and
- Driving channel profitability

Number one is bringing a <u>new Fossil brand platform</u> to life, which we are executing with both strategic and tactical moves. Last month, we went live with a new website, which reflects an elevated product platform focused on watches and innovation. We will also be leveraging the unique skills and competencies at our Innovation Labs in Dallas, Bienne Switzerland, and Hong Kong to develop and deliver exciting new products. In the coming months, we'll be emphasizing heritage brand storytelling across all business dimensions. This will be visible to consumers beginning this summer with the launch of an extensive omnichannel campaign featuring Fossil brand celebrity ambassador Nick Jonas. The campaign is part of our broader strategy to double down on upper funnel tactics to reintroduce the Fossil brand to new and existing customers. As our new Fossil brand platform evolves, we believe there will be an opportunity to expand our pricing architecture, enabling us to extend our reach and further strengthen our position in the traditional watch market.

Turning to our second initiative, leveraging our core licensed brands, we have already made excellent progress. Last month, we announced the extension of our license agreement for Michael Kors. This partnership goes back 20 years and is very important to Fossil Group. We look forward to growing our Kors watch and jewelry business together in the coming years as their company continues to drive a brand turnaround. Next, we have made progress toward achieving minimum royalty reductions with some of our long-time licensed brand partners who we continue to prioritize. Lastly, we are reinvigorating the in-store presentation for our licensed brands within the wholesale channel. This includes greater investments in POS and in-store presentation and a renewed focus on the specialty watch channel.

Optimizing our wholesale global footprint is a third key initiative under our pillar to refocus on our core. We're prioritizing scalable markets, which include the US, Germany, France and India. These are among our most important geographies where we have a strong presence and significant brand awareness. In parallel with our focus on these markets, we have made the strategic decision to transition smaller international geographies within Europe and Asia to a distributor model. This will allow us to build a more competitive and profitable model in key markets. Leveraging the local knowledge and regional expertise of distributors will enable us to lower our operating expenses, enabling strong flow-through of gross profit to the bottom line and positioning us to drive long-term and scalable growth. Thus far, we have transitioned five countries - Denmark, Finland, Norway, Poland and Sweden - and expect to transition additional markets this year.

The final initiative to help us refocus on our core is driving channel profitability. We are deploying a two-pronged approach, which includes prioritizing the wholesale channel and transforming our direct-to-consumer business model.

Starting with wholesale, we are working to improve our in-store presence through enhanced visual merchandising, point of sale displays, and sales education designed to increase the visibility of our brands, improve ease of purchase, and drive conversion. Another critical component of our wholesale strategy is to become increasingly less promotional in our DTC channels. Our initial actions in Q4 have already started to bear fruit, translating to an improving gross margin profile across all channels. We believe this will also help bolster our relationships with our wholesale partners around the globe.

Looking at our direct to consumer business, we believe there is a significant opportunity to strengthen our model, becoming smaller but much more profitable. This starts with delivering a seamless omnichannel experience and creating platforms for personalized journeys that drive strong customer engagement across e-commerce and retail stores.

As I just mentioned, we reduced our e-commerce promotional activity in Q4. In addition to improving our gross margin performance, this also resulted in higher quality traffic to our website, and increased AUR (average unit retail), which has continued in Q1 2025. While this tactic is expected to create a near-term headwind to sales, we anticipate it will drive more profitable growth over the long term.

From a retail store perspective, we aim to strengthen execution by emphasizing traditional watches, highlighting personalization, upgrading our store operating model, and optimizing our fleet with the expected closure of approximately 50 stores in 2025.

Moving now to our **second turnaround pillar** - **rightsizing the cost structure**. As we noted in today's press release, we have made the decision to conclude our TAG program in 2024, which generated approximately $280 million of annualized P&L benefits across gross margin and SG&A over a two-year period. We are now taking action to further align our cost structure to the newly defined strategy, scope and scale we're outlining today. In 2025, we expect to capture SG&A savings of approximately $100 million compared to 2024 through a series of initiatives. This includes a corporate workforce reduction which occurred in late February, reduced costs associated with the transition of smaller international markets to a distributor model, and the closing of approximately 50 Fossil retail stores. We also expect to divest certain non-core assets and will seek to identify additional cost-reduction opportunities, which may generate incremental savings this year.

Wrapping up with our **third turnaround pillar** - **<u>strengthening the balance sheet.</u>** We ended the year with $177 million of liquidity, which provides us with the runway to execute the plans we're outlining today. We are actively working toward monetizing non-core assets, and we're pursuing avenues that will allow us to improve working capital and strengthen liquidity. At the same time, we continue working with our advisors to address our upcoming debt maturities.

We are pleased that the initial actions under our turnaround plan are already beginning to take hold and generate tangible results. There are five major areas of improvement to date I want to highlight:

1. First, we achieved adjusted operating income profitability in Q4 and delivered results ahead of expectations.
2. Second, in Q4, we saw improving performance in our US wholesale business, which has continued into 2025.
3. Next, we brought down promotional levels, which is translating to a higher gross margin profile. In Q4, gross margins expanded 630 basis points versus the prior year to 53.9%.
4. Additionally, we moved swiftly to transition select international markets to a more profitable distributor model, signing agreements for five countries thus far and positioning us to deliver long-term and scalable growth in those geographies.
5. Lastly, we brought in a celebrity ambassador with an incredibly high profile and deep cultural relevance. We believe that our partnership with Nick Jonas and the campaign we're launching in the second half of this year has the potential to really move the needle for the Fossil brand.

We are assembling a powerful leadership bench. Last month, we appointed Joe Martin as our new Chief Commercial Officer to lead our global sales efforts and ensure consistency across brands and regions. The creation of this role is part of a broader organizational redesign to help us execute our brand-led and consumer-focused strategy. We also announced the appointment of Antonio Carriero as Chief Digital Information Officer and General Manager of the EMEA region. Antonio's background in digital and deep knowledge of the watch market will be strong assets to drive an omnichannel experience and strengthen the customer journey. Rounding out our team is Randy Greben, a highly seasoned finance executive who we just announced today as our incoming CFO.

I am incredibly proud of our teams throughout the organization, who have been working fast and furious to generate these results and lay the groundwork for a return to profitable growth. The path to get there is clear. In 2025, we will be resetting the top line, predominantly driven by store closures and lower levels of promotional activity. However, we anticipate that our cost actions, ongoing expense control, and improved gross margin will enable us to narrow our adjusted operating loss on a full-year basis versus 2024.

We believe the new business model we're outlining today will set us up to return to profitable growth in the coming years. In 2026, we expect to be adjusted operating income profitable on a smaller sales base. For the full year in 2027, we expect the business to generate mid-single-digit adjusted operating margins and positive free cash flow on a worldwide net sales base of more than $800 million.

We are committed to the journey ahead and have strong conviction that our turnaround plan will allow us to build long-term shareholder value. We greatly appreciate the support of all of our stakeholders and look forward to keeping you updated on our progress.

Now, I'll turn the call to Andy to review the fourth quarter financial results and provide a more detailed discussion of our financial guidance.

Andrew Skobe, Interim Chief Financial Officer:

Thank you, Franco. Good afternoon, everyone.

We concluded the year with positive adjusted operating income in Q4 despite a year-over-year sales decline. This performance reflects our ability to strengthen our gross margin profile and maintain strict cost control.

Fourth quarter net sales totaled $342 million, down 18% in constant currency. 600 basis points of the decline is attributable to our smartwatch exit and store closures. During the quarter, our Fossil traditional watch business increased 2% globally versus the prior year, excluding store closures. Notably, this positive performance during the holiday season enabled our US wholesale partners to enter 2025 with healthy inventory positions. In fact, after narrowing our sales declines in US wholesale during Q4, the channel continues showing signs of improvement in 2025.

Gross margin expanded by 630 basis points compared to last year, coming in at 53.9%. Gross margin included restructuring charges of approximately $8 million, or 220 basis points, related to the closure of our Swiss manufacturing operations. Excluding these costs, gross margin increased 850 basis points. The year-over-year increase primarily reflects increased product margins in our core categories driven by improved product costing, our exit from connected watches, and reduced promotional activity in our e-commerce business.

SG&A expenses were down $35 million to $172 million compared to last year, representing a 17% decrease from our cost takeout actions. The year-over-year reductions are attributable to:

- Lower store operating costs on fewer stores,
- Lower compensation and administrative expenses, and
- A planned decrease in marketing spend versus the prior year.

During Q4, we closed 6 stores, ending the year with 248 stores, an 18% reduction compared to 2023. All of these closures occurred at natural lease expiration with very minimal closing costs.

Turning now to the bottom line, our focus on gross margin expansion and cost reduction enabled us to deliver fourth-quarter adjusted operating income of $20 million compared to a loss of $8 million a year ago. This strength translated to a Q4 adjusted operating margin of 6%.

Moving to the balance sheet, we ended the year with total liquidity of $177 million, including $124 million in cash and cash equivalents and $53 million of availability under our revolving credit facility. Inventory levels decreased by 29% compared to a year ago, which aligns with our expectations. The business generated positive free cash flow of $30 million in Q4, primarily reflecting the reduction in inventory. As we execute the turnaround plan Franco outlined we are working to strengthen the balance sheet and increase liquidity in 2025. In parallel, we are pursuing non-core asset sales and opportunities to achieve incremental expense savings while also continuing to work with our advisors on our previously announced Strategic Business Review.

Turning now to guidance. For the full year in 2025, we expect worldwide net sales to decline in the mid to high teens. This includes an expected impact from store closures of approximately $45 million, or 4 percentage points. We also anticipate an impact to sales from our reduced promotional levels, particularly in our owned e-commerce channel. Of note, this guidance excludes impacts from changes to foreign currency exchange rates, potential asset sales or a further softening of the macro environment. As we think about the cadence of sales, we anticipate that our initiatives will gain increasing traction and enable us to narrow our year-over-year sales declines as we move through the year.

Looking at gross margin, as we focus on driving a full-price selling model, we expect to see continued improvement in gross margin versus full year 2024. Additionally, in the first half of the year, we expect to see flow through from the annualized benefits of our sourcing initiatives. From a tariff perspective, based on what we know today and our scenario planning, we do not anticipate a material gross margin impact.

As Franco mentioned, we are taking actions this year that are expected to generate approximately $100 million of SG&A expense savings in 2025 versus 2024. Three factors are driving the savings.

1. First, we implemented a corporate reduction in force last month,
2. Next, we expect to continue to rationalize the store portfolio, with plans to close approximately 50 stores in 2025, and
3. Third, we transitioned five international markets to a distributor model, which brings our operating costs in those markets to near zero.

The expected savings do not contemplate additional international regions that may be transitioned to a distributor model in 2025 or the potential sale of non-core assets.

We anticipate these factors will enable us to deliver a full-year adjusted operating margin in the negative low single digits.

We appreciate your time this afternoon and will be available for follow-up calls. Now, I'll turn the call back to Franco for closing comments.

Franco Fogliato, Chief Executive Officer:

Thank you, Andy. I'd also like to take the opportunity to thank you for the value you've added during your interim time with the organization and wish you the best going forward.

I am inspired by our teams who are demonstrating tremendous dedication to Fossil and commitment to turning around this business. We are all energized by the opportunity in front of us and look forward to keeping you updated on our progress throughout the year as we strive to build lasting value for our shareholders.